

REPORT OF THE AUDITOR-GENERAL TO THE NORTHERN CAPE PROVINCIAL LEGISLATURE AND THE COUNCIL ON GAMAGARA LOCAL MUNICIPALITY

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I have audited the financial statements of the Gamagara Local Municipality set out on pages ... to ..., which comprise the statement of financial position as at 30 June 2013, the statement of financial performance, statement of changes in net assets, the statement of comparison of the budget and actual amounts and the cash flow statement for the year then ended, and the notes, comprising a summary of significant accounting policies and other explanatory information.

Accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and Division of Revenue Act of South Africa, 2012 (Act No. 5 of 2012) (DoRA) and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor-General's responsibility

3. My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), the general notice issued in terms thereof and International Standards on Auditing. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.
4. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified audit opinion.

Basis for qualified opinion

Property, plant and equipment

6. The municipality did not disclose property plant and equipment in accordance with the Standard of Generally Recognised Accounting Practice, GRAP 17, *Property, plant and equipment*. Property plant and equipment stated at R1 066 509 121 (2012: R1 035 311 772) in note 8 to the financial statements were misstated due to the following matters:
- Property plant and equipment are overstated by R35 679 400 as land was disclosed that does not belong to the municipality.
 - Property plant and equipment are overstated by R170 856 as buildings were disclosed that do not belong to the municipality.
 - Property, plant and equipment are overstated by R83 379 364 as a result of duplicated land disclosed.
 - Investment property of R11 503 652 (2012: R382 361) was incorrectly disclosed as property plant and equipment.
 - The municipality did not review the residual values and useful lives of property plant and equipment at each reporting date in accordance with the Standard of Generally Recognised Accounting Practice, GRAP 17, *Property, plant and equipment*. I was not able to determine the correct net carrying amount of these assets as it was impracticable to do so.
 - In addition, property plant and equipment of R6 058 358 that were damaged during the protests in Olifantshoek were not impaired.
7. In addition, I was unable to obtain sufficient appropriate audit evidence for journals processed against property plant and equipment, as the municipality did not have adequate systems in place to maintain records of journals processed. I was unable to confirm these journals processed by alternative means. Consequently, I was unable to determine whether any adjustments to property plant and equipment were necessary.

Cash flow statement

8. I was unable to obtain sufficient appropriate audit evidence for net cash flows from operating activities stated as R57 709 364 (2012: R36 567 347) in the cash flow statement. I was unable to confirm this line item by alternative means. Consequently, I was unable to determine whether any adjustments to this line item were necessary.

Commitments

9. I was unable to obtain sufficient appropriate audit evidence for commitments disclosed as R81 845 974 (2012: R24 366 425) in note 46 to the financial statements. The municipality did not have adequate systems in place to maintain records of commitments. I was unable to confirm these commitments by alternative means. Consequently, I was unable to determine whether any adjustments to commitments were necessary.

Irregular expenditure

10. The municipality did not include particulars of irregular expenditure in the notes to the financial statements as required by section 125 of the Municipal Finance Management Act. The municipality made payments in contravention of the supply chain management requirements which were not included in irregular expenditure disclosed, resulting in

irregular expenditure being understated by R36 367 984 (2012: R R40 829 446).

11. In addition, the municipality did not have adequate systems in place to maintain records of transactions relating to irregular expenditure and could not submit all procurement documentation that were requested as well as evidence that investigations were done as required by section 32(2)(b) of the Municipal Finance Management Act . I was unable to confirm irregular expenditure by alternative means. Consequently, I was unable to determine whether any adjustments to irregular expenditure were necessary.

Distribution losses

12. Distribution losses for electricity was not disclosed, as required by section 125(2d)(i) of the Municipal Finance Management Act in note 45.8 to the financial statements. I was not able to determine the amount of these losses as it was impracticable to do so.

Qualified opinion

13. In my opinion, except for the possible effects of the matters described in the Basis for qualified opinion paragraphs, the financial statements present fairly, in all material respects, the financial position of the Gamagara Local Municipality as at 30 June 2013 and its financial performance and cash flows for the year then ended, in accordance with SA Standards of GRAP and the requirements of the MFMA and DoRA.

Emphasis of matters

14. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Restatement of corresponding figures

15. As disclosed in note 41 to the financial statements, the corresponding figures for 30 June 2012 have been restated as a result of an error discovered during 2013 in the financial statements of the Gamagara Local Municipality at, and for the year ended, 30 June 2012.

Material losses and impairments

16. As disclosed in the statement of financial performance, material losses of R6,8 million (2012: R1,8 million) were incurred as a result of a write-off of irrecoverable trade debtors.
17. As disclosed in note 4 to the financial statements, the municipality had receivables for exchange transactions of R36,7 million at 30 June 2013. An amount of R20,2 million is disclosed as a provision for impairment.

Additional matters

18. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Material inconsistencies in other information included in the annual report

19. I have not obtained the other information included in the annual report. Consequently, I have not been able to determine whether the other information to be included in the annual report contains any material inconsistencies with the information in the financial statements.

Unaudited supplementary schedules

20. The supplementary information set out on pages XX to XX does not form part of the financial statements and is presented as additional information. I have not audited these schedules and accordingly, I do not express an opinion thereon.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

In accordance with the PAA and the general notice issued in terms thereof, I report the following findings relevant to performance against predetermined objectives, compliance with laws and regulations and internal control, but not for the purpose of expressing an opinion.

Predetermined objectives

21. I performed procedures to obtain evidence about the usefulness and reliability of the information in the annual performance report as set out on pages ... to ... of the annual report.
22. The reported performance against predetermined objectives was evaluated against the overall criteria of usefulness and reliability. The usefulness of information in the annual performance report relates to whether it is presented in accordance with the National Treasury's annual reporting principles and whether the reported performance is consistent with the planned development priorities. The usefulness of information further relates to whether indicators and targets are measurable (i.e. well defined, verifiable, specific, measurable and time bound) and relevant as required by the National Treasury *Framework for managing programme performance information*.

The reliability of the information in respect of the selected development priorities is assessed to determine whether it adequately reflects the facts (i.e. whether it is valid, accurate and complete).

23. The material findings are as follows:

Usefulness of information

24. Section 46 of the Municipal Systems Act requires disclosure in the annual performance report of measures taken to improve performance where planned targets were not achieved. Measures to improve performance for a total of 93% of the planned targets not achieved were not reflected in the annual performance report. This was due to the lack of processes put in place by the municipality to ensure that the annual performance report includes all the required information.
25. The Municipal Systems Act, section 41(c) requires that the integrated development plan should form the basis for the annual report, therefore requiring consistency of objectives, indicators and targets between planning and reporting documents. The following inconsistencies were identified:
 - A total of 86% of the reported objectives are not consistent with the objectives as per the approved integrated development plan.
 - A total of 24% of reported indicators are not consistent with the indicators as per the approved integrated development plan.
 - A total of 59% of the reported targets are not consistent with the targets as per the approved integrated development plan.

This is due to the lack of proper processes put in place by the municipality to ensure that information included in the annual performance report is consistent with all planning documents.

26. The Municipal Systems Act, section 41(c) requires that the actual achievements against all planned indicators and targets must be reported annually. The annual performance

report submitted for audit purposes did not include the actual performance of 24% of all planned objectives, indicators and targets specified in the integrated development plan for the year under review. This was due to limited information systems recording and documenting of actual achievements against targets as well as limited review and monitoring of the completeness of reporting documents by management, audit committee and internal audit.

27. The National Treasury Framework for managing programme performance information requires that performance targets be specific in clearly identifying the nature and required level of performance. A total of 100% of the targets in relation to Development priority 1: Provision of basic services and waste management were not specific in clearly identifying the nature and the required level of performance. This was due to the fact that management was aware of the requirements of the National Treasury Framework for managing programme performance information but chose not to apply the principles contained in the National Treasury Framework for managing programme performance information.
28. The National Treasury Framework for managing programme performance information requires that performance targets be measurable. The required performance could not be measured for a total of 100% of the targets in relation to Development priority 1: Provision of basic services and waste management. This was due to the fact that management was aware of the requirements of the National Treasury Framework for managing programme performance information but chose not to apply the principles contained in the National Treasury Framework for managing programme performance information.
29. The National Treasury Framework for managing programme performance information requires that the time period or deadline for delivery be specified. A total of 100% of the targets in relation to Development priority 1: Provision of basic services and waste management of the targets were not time bound in specifying a time period or deadline for delivery. This was due to the fact that management was aware of the requirements of the National Treasury Framework for managing programme performance information but chose not to apply the principles contained in the National Treasury Framework for managing programme performance information.
30. The National Treasury Framework for managing programme performance information requires that indicators and measures should have clear unambiguous data definitions so that data is collected consistently and is easy to understand and use. A total of 100% of the indicators in relation to Development priority 1: Provision of basic services and waste management were not well defined in that clear, unambiguous data definitions were not available to allow for data to be collected consistently. This was due to the fact that management was aware of the requirements of the National Treasury Framework for managing programme performance information but chose not to apply the principles contained in the National Treasury Framework for managing programme performance information.
31. The National Treasury Framework for managing programme performance information requires that it must be possible to validate the processes and systems that produce the indicator. A total of 100% of the indicators in relation to Development priority 1: Provision of basic services and waste management were not verifiable in that valid processes and systems that produce the information on actual performance did not exist. This was due to the lack of key controls in the relevant systems of collection, collation, verification and storage of actual performance information, and management was aware of the requirements of the National Treasury Framework for managing

programme performance information but chose not to apply the principles contained in the National Treasury Framework for managing programme performance information.

Reliability of information

32. The National Treasury Framework for managing programme performance information requires that institutions should have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. I was unable to obtain the information and explanations I considered necessary to satisfy myself as to the reliability of information presented with respect to Development priority 1: Provision of basic services and waste management.
33. This was due to limitations placed on the scope of my work because of the absence of an information system and the fact that the institution could not provide sufficient appropriate evidence in support of the information presented with respect to the development priority.

Additional matter

34. I draw attention to the following matter. This matter does not have an impact on the predetermined objectives audit findings reported above.

Achievement of planned targets

35. I could not determine the achievement of planned targets as the targets reported in the annual performance report did not agree to the planned targets, as set out in the approved integrated development plan.

Compliance with laws and regulations

36. I performed procedures to obtain evidence that the municipality had complied with applicable laws and regulations regarding financial matters, financial management and other related matters. My findings on material non-compliance with specific matters in key applicable laws and regulations, as set out in the general notice issued in terms of the PAA, are as follows:

Strategic planning and performance management

37. The municipality did not maintain effective, efficient and transparent systems of financial and risk management and internal controls as required by section 62(1) (c) (i) of the Municipal Finance Management Act.
38. The performance management system of the municipality was not in line with the priorities, objectives, indicators and targets contained in its integrated development plan, did not clarify the roles and responsibilities of each role-player in the functioning of the system, did not determine the frequency of reporting and the lines of accountability for performance, did not relate to the municipality's performance management processes and did not provide for procedures by which the system is linked to the municipality's integrated development planning processes, as required by section 38(a) of the Municipal Systems Act and Municipal planning and performance management regulation 7(2).
39. The performance management system of the municipality did not provide for the monitoring of performance and for the measuring and review of performance at least once per year, with regard to each of those development priorities and objectives and against the key performance indicators and targets set, as required by section 41 of the Municipal Systems Act.

40. The municipality did not set key performance indicators, including input indicators, output indicators and outcome indicators, in respect of each of the development priorities and objectives set out in the integrated development plan, as required by section 41(1)(a) of the Municipal Systems Act and the Municipal planning and performance management regulation 1 and 9(1)(a).
41. The internal audit unit did not assess the functionality of the performance management system, whether the performance management system complied with the requirements of the Municipal Systems Act, the extent to which the performance measurements were reliable in measuring the performance of the municipality on key and general performance indicators, as required by Municipal Planning and Performance Management Regulation 14(1)(b).
42. The internal audit unit did not assess the extent to which the performance measurements were reliable in measuring the performance of the municipality on key and general performance indicators, as required by Municipal planning and performance management regulation 14(1)(b)(iii).
43. The internal audit unit did not audit the performance measurements on a continuous basis nor submitted quarterly reports on their audits to the municipal manager and the performance audit committee, as required by Municipal Planning and Performance Management Regulation 14(1)(c).
44. Annual performance report for 2012-13 did not contain a comparison of the performance of the municipality and of each external service provider with development priorities, objectives and performance indicators set out in its integrated development plan as required by section 46(2) of the Municipal Systems Act.
45. The annual performance report for the year under review does not include the performance of the municipality and of external service providers, a comparison of the performance with set targets, a comparison with the previous financial year and measures taken to improve performance, as required by section 46 of the Municipal Systems Act.

Budget

46. Expenditure was incurred in excess of the limits of the amounts provided for in the votes of the approved budget, in contravention of section 15 of the Municipal Finance Management Act.

Financial statements, performance and annual reports

47. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the Municipal Finance Management Act. Material misstatements of non-current assets, current assets, liabilities, revenue, expenditure and disclosure items identified by the auditors in the submitted financial statements were corrected and the supporting documentation were provided subsequently, but the uncorrected material misstatements and supporting documentation that could not be provided resulted in the financial statements receiving a qualified audit opinion.

Audit committee

48. The audit committee did not advise the council and accounting officer on matters relating to the adequacy, reliability and accuracy of financial reporting and information, as required by section 166(2)(a)(iv) of the Municipal Finance Management Act.

49. The audit committee did not advise the council and accounting officer on matters relating to compliance with legislation, as required by section 166(2)(a)(vii) of the Municipal Finance Management Act.
50. The audit committee did not review the annual financial statements to provide the council with an authoritative and credible view of the financial position of the entity, its efficiency and effectiveness and its overall level of compliance with legislation, as required by section 166(2)(b) of the Municipal Finance Management Act.
51. The audit committee did not respond to the council on the issues raised in the audit reports of the Auditor-General, as required by section 166(2)(c) of the Municipal Finance Management Act.
52. The audit committee did not advise the council on matters relating to accounting policies and effective governance as required by section 166(2)(a) of the Municipal Finance Management Act.

Internal audit

53. The internal audit unit did not report to the audit committee on matters relating to compliance with the Municipal Finance Management Act, Division of Revenue Act and other applicable legislation, as required by section 165(2)(b) of the Municipal Finance Management Act.

Procurement and contract management

54. Goods and services with a transaction value of below R200 000 were procured without obtaining the required price quotations, as required by Supply Chain Management regulation 17(a) and (c).
55. Sufficient appropriate audit evidence could not be obtained that goods and services of a transaction value above R200 000 were procured by means of inviting competitive bids or that deviations approved by the accounting officer were only if it was impractical to invite competitive bids, as required by Supply Chain Management regulations 19(a) and 36(1).
56. Sufficient appropriate audit evidence could not be obtained that bid specifications for procurement of goods and services through competitive bids were drafted in an unbiased manner that allowed all potential suppliers to offer their goods or services, as required by Supply Chain Management regulation 27(2)(a).
57. Bid specifications were not always drafted by bid specification committees which were composed of one or more officials of the municipality as required by Supply Chain Management regulation 27(3).
58. Invitations for competitive bidding were not always advertised for the required minimum period of days, as required by Supply Chain Management regulation 22(1) and 22(2).
59. Sufficient appropriate audit evidence could not be obtained that bids were evaluated by bid evaluation committees which were composed of officials from the departments requiring the goods or services and at least one Supply Chain Management practitioner of the municipality, as required by Supply Chain Management regulation 28(2).
60. Bid adjudication was not always done by committees which were composed in accordance with Supply Chain Management regulation 29(2).
61. Sufficient appropriate audit evidence could not be obtained that contracts and

quotations were awarded to and accepted from suppliers based on preference points that were allocated and calculated in accordance with the requirements of the Preferential Procurement Policy Framework Act and its regulations.

62. The performance of contractors or providers was not monitored on a monthly basis, as required by section 116(2)(b) of the Municipal Finance Management Act.
63. Construction projects were not always registered with the Construction Industry Development Board (CIDB), as required by section 22 of the CIDB Act and CIDB regulation 18.
64. Contracts were awarded to providers whose tax matters had not been declared by the South African Revenue Service to be in order, as required by Supply Chain Management regulation 43.
65. Sufficient appropriate audit evidence could not be obtained that all contracts and quotations were awarded in accordance with the legislative requirements and a procurement process which is fair, equitable, transparent and competitive. This was due to inadequate record management.
66. The prospective providers list for procuring goods and services through quotations was not updated at least quarterly to include new suppliers that qualify for listing, and prospective providers were not invited to apply for such listing at least once a year as per the requirements of Supply Chain Management regulation 14(1)(a)(ii) and 14(2).

Expenditure management

67. Reasonable steps were not taken to prevent irregular, unauthorised, fruitless and wasteful expenditure, as required by section 62(1)(d) of the Municipal Finance Management Act.

Assets management and liability management

68. An effective system of internal control for assets was not in place, as required by section 63(2)(c) of the Municipal Finance Management Act.
69. The municipality did not establish an investment policy that was adopted by council, as required by section 13(2) of the Municipal Finance Management Act and Municipal investment regulation 3(1)(a).

Consequences management

70. Sufficient appropriate evidence could not be obtained that unauthorised expenditure incurred by the municipality was investigated to determine whether any person was liable for the expenditure in accordance with the requirements of section 32(2) of the Municipal Finance Management Act.
71. Sufficient appropriate evidence could not be obtained that irregular expenditure incurred by the municipality was investigated to determine whether any person was liable for the expenditure in accordance with the requirements of section 32(2) of the Municipal Finance Management Act.
72. The condoning of irregular expenditure was not approved by the appropriate relevant authority, in accordance with the requirements of sections 1 and 170 of the Municipal Finance Management Act.

73. Unauthorised, irregular, fruitless and wasteful expenditure was not always recovered from the liable person, as required by section 32(2) of the Municipal Finance Management Act.
74. Sufficient appropriate evidence could not be obtained that unauthorised, irregular, fruitless and wasteful expenditure was only written off as irrecoverable if certified by council as irrecoverable, as required by section 32(2) of the Municipal Finance Management Act.

Internal control

75. I considered internal control relevant to my audit of the financial statements, annual performance report and compliance with laws and regulations. The matters reported below under the fundamentals of internal control are limited to the significant deficiencies that resulted in the basis for qualified opinion, the findings on the annual performance report and the findings on compliance with laws and regulations included in this report.

Leadership

76. The leadership did not exercise oversight of property, plant and equipment by ensuring that adequate internal controls were in place to ensure that all machinery and equipment are recorded in the asset register.
77. The leadership did not evaluate whether management had implemented effective internal controls by gaining an understanding of how senior management had met their responsibilities.
78. The leadership did not ensure adherence to supply chain management policy at the municipality, which resulted in processes not preventing irregular expenditure and material non-compliance.
79. The leadership did not review and monitor performance information and compliance with applicable laws and regulations.

Financial and performance management

80. Reconciliations, reviews and monitoring were not always performed by the management, which led to material amendments to the financial statements.
81. Management did not perform a proper review on the financial statements compiled by external service providers, which resulted in material amendments to the financial statements to ensure fair presentation of the financial statements.
82. The systems underlying the procurement processes at the municipality were inadequate to prevent and detect irregular expenditure on contracts entered into, resulting in irregular expenditure that was disclosed in the accounting records of the municipality. Effective and appropriate disciplinary steps were not taken against officials who made and permitted unauthorised, irregular and fruitless and wasteful expenditure.
83. The municipality did not have a delegated employee to review and monitor compliance with applicable laws and regulations. There are deficiencies in the design and implementation of internal control in respect of compliance with applicable laws and regulations and performance information.
84. The underlying systems and controls were inadequate to provide reliable and accurate

evidence to support reporting on predetermined objectives. Senior management did not perform an adequate review on the actual performance against predetermined objectives reported; therefore no explanations were documented for targets that were not achieved.

Governance

85. The municipality did not adequately identify risks relating to the IT environment and the achievement of financial and performance reporting objectives. Consequently, controls were not developed to prevent, detect and correct material misstatements in financial reporting and reporting on predetermined objectives.
86. The municipality utilised the shared internal audit division and audit committee within the John Taolo Gaetsewe District Municipality. The audit committee did not review the performance management systems and did not make recommendations to the councils in this regard. In addition the internal audit division did not report on compliance with laws and regulations.

Auditor General,

Kimberley

30 November 2013



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence